

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

POSTAL RATE AND FEE CHANGES, 2001

Docket No. R2001-1

REPLY BRIEF OF THE
UNITED STATES POSTAL SERVICE

UNITED STATES POSTAL SERVICE

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I. Introduction.

In Part V of its Initial Brief, the United States Postal Service explained why the Commission should recommend the First-Class Mail rate design proposed in the Stipulation and Agreement. Because the Postal Service's position was presented in such detail in that brief, the Postal Service will not attempt to repeat its earlier arguments.¹ Instead, for the most part, appropriate views are expressed in this brief in the context of responding to the specific arguments in the parties' briefs.

In its brief opposing the First-Class Mail rate design in the Stipulation and Agreement, the American Postal Workers Union, AFL-CIO (APWU) argues that, based upon the testimony of APWU witness Riley (Tr. 12/4840 *et seq.*), the Commission should not recommend discounts for workshare rate categories and QBRM that exceed the workshare cost avoidance estimates presented by the Postal Service. APWU also

¹ In terms of the rates for all other classes, the Postal Service appreciates the widespread support for the settlement rates, as expressed by the participants in their initial briefs. The Postal Service does not, however, endorse some of the *post hoc* justifications offered by some of the participants on brief in support of the settlement rate and classification changes. For instance, the Postal Service disagrees with Val-Pak's suggestion on brief that the extension of the "heavy letter" rate treatment to the ECR subclass is somehow mandated by the nondiscrimination provisions of 39 USC 403(c). Val-Pak Initial Brief at 10-13. The Commission does not need to speculate about the proper interpretation of section 403(c), particularly since the participants have not had the opportunity to offer evidence in support of, and in rebuttal to, this erroneous interpretation of section 403(c). In addition, the Postal Service does not accept NAA's suggestion on brief that record evidence is somehow "more consistent" with the settlement on the ECR pound rate than the Postal Service's larger proposed ECR pound rate reduction. NAA Initial Brief at 2. To the contrary, the Postal Service submits that the record amply supports the ECR pound rate reduction on the order of magnitude proposed by the Postal Service. The Commission should accordingly refrain from drawing such conclusions about the nature of the evidence supporting the pound rate reduction.

argued against the proposed reduction in the additional-ounce rate for workshare letters. In support of the First-Class Mail rate design reflected in the Stipulation and Agreement, other parties or coalitions of parties² make arguments to which the Postal Service also is impelled to respond below.

II. The Commission Should Summarily Dismiss APWU Arguments Based On Improper Extra-Record Material.

Referencing the Fiscal Year 2001 Annual Report of the United States Postal Service at page 9 of its Initial Brief, APWU makes a number of arguments based upon speculation regarding postal finances, revenues, and capital investment plans for FY 2002 and test year, as well as the parameters of the next rate case. It should be apparent to the Commission that there is no record basis for these arguments. The Commission may be authorized by Rule 31(j) of its Rules of Practice and Procedure to take official notice of facts contained in that Annual Report, but that report provides no basis for APWU's speculation about FY 2002 and the test year. Accordingly, the arguments at pages 9-13 of the APWU Brief must be summarily dismissed.

The testimony of APWU witness Riley (Tr. 12/4840 *et seq.*) does not dispute the Postal Service's test year roll-forward cost estimates or its requested revenue requirement. The Commission will be hard-pressed to find testimony by APWU witness Riley on such matters as the Postal Service's test year debt ceiling or capital investment

² American Bankers Association & National Association of Presort Milers (ABA&NAPM); KeySpan Corporation, Automatic Data Processing, Electronic Data Services, and Long Island Power Authority (hereinafter, KeySpan *et al.*); and Major Mailers Association (MMA).

plans, which are discussed on pages 10 and 11 of APWU's Initial Brief. Nor did he testify about the potential magnitude of "the next rate case."³ Although witness Riley expressed concerns about what he characterized as the "dire financial straits" of the Postal Service,⁴ he conceded that "[u]pdated financial information has not been added to the record in this case"⁵ As stated in its brief, "APWU decided . . . to challenge only the First-Class Mail discounts." APWU Initial Brief at 1, n.1. In fact, APWU concedes that its January 15, 2002, notice of opposition to the Stipulation and Agreement was "limited to the rate designed proposed for First-Class Mail . . . because the proposed discounts exceeded cost avoidance." *Id.* APWU also acknowledges that its notice of opposition "sets the parameters of the contested issues in this case." *Id.*

As discussed above, witness Riley's testimony offered a cryptic qualitative characterization of postal finances. At most, he provided what he characterized as a "guess" about how much the Postal Service's test year revenue requirement might have changed if, in response to the events that led to pursuit of the Stipulation and Agreement, the Postal Service had updated its roll-forward cost estimates and revenue requirement. Tr. 12/4946. Otherwise, when pressed for an estimate of the revenue impact of his own alternate rate design proposal, he turned it up a notch and provided an "educated guess." Tr. 12/4898-99.

³ See APWU Initial Brief at 11.

⁴ Tr. 12/4848.

⁵ *Id.*

At page 9 of its Initial Brief, APWU argues that “given this unprecedented set of circumstances, the Commissioners should consider the current financial situation of the Postal Service.” Yet, no party, including APWU, has offered anything resembling an alternative test year financial forecast that contradicts the Postal Service’s testimony. The Postal Service submits that, given the unprecedented set of circumstances to which APWU alludes, the Commission should more properly focus on the financial benefits that will accrue to the Postal Service as a result of the its recommendation of the rate and classification changes reflected in the Stipulation and Agreement.

III. APWU Confuses The Issues, Ignores Precedent, and Misconstrues The Record.

A. APWU Misunderstands the Relationship Between Institutional Cost Allocation and Subclass Rate Design.

Within the iterative ratemaking process in which the test year revenue requirement is projected and test year volumes, costs, and revenues for each subclass are estimated, one of the most critical steps is the allocation of institutional costs among the various subclasses, in accordance with the criteria in section 3622(b) of the Postal Reorganization Act. The objective of this exercise, besides rates which satisfy the criteria of the Act, is to meet the requirement in section 3621 that postal test year revenues and expenses are as close to breakeven as is practicable. PRC Op. MC95-1 at III-23, ¶3059. The Stipulation and Agreement under consideration in Docket No. R2001-1 builds upon the uncontested application of the section 3622(b) ratemaking criteria in Postal Service witness Moeller’s testimony (USPS-T-28) and results in a fair and equitable distribution of the burden of test year institutional costs among the mail

classes to achieve this objective. The allocation of institutional cost reflected in the Stipulation and Agreement is not explicitly contested by APWU.

As a result of this institutional cost allocation process, each subclass is assigned a test year revenue target that must be met by the rates collectively paid by the mail pieces in the subclass. Postal Service witness Robinson (USPS-T-29) had the responsibility of designing a mix of rates for the various First-Class Mail rate categories and rate elements in each First-Class Mail subclass that would generate sufficient revenue to meet the revenue target for each subclass. Her rate design accomplished that objective. Although the impact of the Stipulation and Agreement was to adjust the revenue generated by only a few rate categories within the Letters and Cards subclasses, neither the original rate design nor the stipulated rate design generates First-Class Mail revenue in excess of the specific subclass targets established by witness Moeller (USPS-T-28). In fact, by proposing slightly smaller rates increases for the Automation 3-Digit, Automation 5-Digit Presort, and QBRM letter and card rate categories, the Stipulation and Agreement shrinks the overall test year revenue requirement requested by the Postal Service, by reducing the First-Class Mail revenue goal that originally served as witness Robinson's rate design revenue target.

The Postal Service provides this overview because it is apparent that APWU, from the outset, completely misunderstands the rate design process. At page 3 of its Initial Brief, APWU argues that, because the Stipulation and Agreement contains First-Class Mail workshare discounts that exceed witness Miller's estimates of workshare cost avoidance (USPS-T-22), the resulting rate design "requir[es] all First-Class mailers to pick up an added share of institutional cost" However, as the Commission is

well aware, this is simply not the case. As explained above, the aggregate test year institutional cost burden assigned by witness Moeller to First-Class Mail is not increased -- either by the witness Robinson's rate design, or the rate design reflected in the Stipulation and Agreement.⁶

B. Workshare Discount Rate Design Is Not Simply A Mechanistic Exercise.

In Docket No. MC95-1, the Commission considered a Postal Service proposal to split the Letters and Cards subclasses each into two distinct subclasses, "Retail" and "Automation." In the course of explaining why it would not recommend those proposed reclassifications, the Commission reiterated its views on the criteria for consideration of the establishment of new subclasses and the appropriate bases for the establishment of rate categories within those subclasses. See *generally*, PRC Op. MC95-1 at III-7-31, ¶¶3019-3080.

During the course of its explication, the Commission addressed the issue of the application of the requirement in section 3622(b)(3) that the aggregate revenues generated by the rates for a subclass either equal or exceed the estimated volume variable costs for that subclass. *Id.* at III-8, ¶3020.⁷ The Commission emphasized that the subsection (b)(3) cost floor requirement applied only at the aggregate subclass level during the institutional cost allocation process, not in the rate design process. *Id.* at

⁶ And, as explained above, the stipulated rate design would have the effect of reducing the revenue burdens of the affected First-Class Mail subclasses below those originally requested.

⁷ The cost coverage for a subclass -- the degree to which its revenues exceed its volume variable costs -- is the product of the institutional cost allocation exercise process performed, in the instant docket, by Postal Service witness Moeller (USPS-T-28), who did so by also taking into account the remaining criteria in section 3622(b).

¶3021. It acknowledged that the wide variety of worksharing discounts then in existence gave recognition to subsection (b)(6) policy of recognizing the “degree of preparation of mail . . . performed by the mailer and its effect upon reducing costs to the Postal Service.” *Id.* at III-7, n.3. The Commission then provided an overview of the degree to which cost considerations could influence rate design at the rate category level. It indicated that “rate categories are customarily priced as discounts from their subclass rates, based upon savings from worksharing by mailers. . . .” [Footnote omitted.] *Id.* at III-8, ¶3021. After a digression, the Commission returned to the subject of the impact of cost on rate design, by discussing the goal of pricing workshare discounts in a manner that promoted productive efficiency, in accord with the principles of efficient component pricing. *Id.* at III-29, ¶3074.

Notwithstanding the arguments in the APWU Brief, the Commission has not expressed the view that workshare discount passthroughs cannot exceed 100 percent. The Postal Service does not disagree with the notion that the design of rates for workshare discounts can and, where possible, should take into account the general goal of promoting or encouraging efficiency. However, the Commission also has indicated that particular circumstances can dictate that other principles be given more weight. The Postal Service concurs. Although, as indicated in the preceding paragraph, the Commission has opined that discounts should be based on estimates of cost avoidance, it has never said that discounts were restricted to those estimates.

In response to witness Riley's exhortation that the Commission mechanistically design rates to achieve the goals of efficient of component pricing,⁸ Postal Service witness Moeller provided evidence of the Commission's recent history of taking into account other compelling considerations in workshare rate design. Tr. 13/4970-71. In the first of two examples from Docket No. R2000-1 cited by witness Moeller, the Commission recommended workshare discount passthroughs ranging from 107.5 percent to as high as 199.5 percent, "to avoid rate shock in adversely affected rate categories" within Standard Nonprofit Enhanced Carrier Route Mail. PRC Op. R2000-1 at 331, ¶5372. The second example involved a Commission recommendation of passthroughs in excess of 100 percent explicitly to avoid undue rate increases for Standard Automation Flats, in relation to other rate categories. PRC Op. MC95-1 at 349-50, ¶5142. In each instance, consideration of the impact on mailers, consistent with the principles of section 3622(b)(4), was paramount.

Closer to home is the example of the Commission's treatment of the discount for First-Class Mail Nonautomation Presort letters in Docket No. R2000-1. There, the Commission recommended a discount of 2.0 cents, based on a workshare cost avoidance estimate of 0.4 cents, resulting in a 500 percent passthrough. PRC Op. R2000-1 at 243, Table 5-3. As a result of the Docket No. R2000-1 modification decision of the Governors,⁹ that discount was reduced to 1.8 cents, shrinking the

⁸ He then goes further to advocate reducing all workshare discounts to 80 percent of measured cost avoidance to maximize postal revenues. Tr. 12/4848-49.

⁹ Decision of the Governors of the United States Postal Service on the Recommended Decision on Further Reconsideration of the Postal Rate Commission on Postal Rate and Fee Changes, Docket No. R2000-1 (May 7, 2001).

passthrough to 450 percent. By way of comparison, the proposed Docket No. R2001-1 First-Class Mail workshare passthroughs being challenged by APWU are all in the range of 120 percent, far below various passthroughs that the Commission itself recommended for approval by the Governors in the most recent omnibus rate case.

Unlike the mandate in section 3622(b)(3), which establishes a cost-based standard in the allocation of institutional costs, there is no similarly strict statutory cost-based principle governing rate design within a subclass. Rate design for workshare rate categories is influenced primarily by consideration of the policies underlying sections 3622(b)(6) and (b)(7).¹⁰ Neither provision has been interpreted by the Commission to require rigid adherence to the goals of efficient component pricing, to the exclusion of all other considerations, or to require that efficiency concerns trump all others in rate design.

At page 9 of its Brief, APWU argues that:

the Commission has determined that setting a discount of no more than the cost avoided to recognize worksharing cost distinctions “is most fair and equitable to all mailers.” MC95-1 at [3079].”

This assertion that rigid limits on passthroughs “is most fair and equitable” sounds compelling. And, attributing it to the Postal Rate Commission certainly even gives it a ring of authority. However, this is not what the quoted passage actually says at all. When one reads the complete sentence from which the quote in the above passage is

¹⁰ These provisions, respectively, require consideration of the degree of pre-mailing preparation that reduces postal costs in rate design and the establishment of identifiable rate relationships among mail categories.

taken,¹¹ and puts that complete sentence in the context of the discussion in which it was made, it becomes indisputably clear that APWU -- at least -- has misread the Commission's opinion. All the Commission said in ¶3079 was that, based on the Docket No. MC95-1 record, when choosing between whether to recommend the proposed Retail/Automation First-Class Mail subclass split proposed by the Postal Service, or to recognize the value of worksharing through discounted rate categories from the basic First-Class Mail rate in a unified subclass, the Commission considered the latter approach "most fair and equitable."

On the subject of rate design, more recently the Commission in Docket No. R2000-1 had occasion to consider implicit markups within a subclass in the design of the pound rate in Standard Mail. The Commission opined that its understanding of the rate design issue was advanced by the provision of estimates of implicit markups. PRC Op. R2000-1 at 392, ¶5539. The Commission also declared that it "tries to achieve 100 percent passthrough of the workshare savings, but again it frequently may depart from this standard for a variety of reasons. . . ." *Id.* at 390, ¶5535. The Commission also stated that:

[s]ubclass rate designs proposed by the Postal Service and recommended by the Commission frequently depart from the principle of . . . [efficient component pricing] in order to mitigate the effect of large changes in cost on affected rate payers[, and] . . . to accommodate Postal Service policies concerning how it wants mail prepared[.]

Id. at 391, ¶5538.

¹¹ The sentence in question reads: "Consequently, the most important reason for using a discount approach to recognize cost distinctions brought about by worksharing is that the Commission has determined that this is most fair and equitable to all mailers." PRC Op. MC95-1 at III-312, ¶3079.

As Docket No. R2001-1 First-Class Mail rate design witness Robinson testified, the Postal Service's departure from 100 percent passthroughs in the current case was motivated both by a desire to mitigate the impact of otherwise relatively steep rate increases for workshare mailers and out of concern that a sudden, sharp decrease in discounts could cause an undesirable diminution in the level of level mailer worksharing, to the detriment of postal automation goals. USPS-T-29 at 10-13. *See also*, Tr. 10/2837-38.

APWU may believe that such considerations are inconsistent with the requirements of "good business management." APWU Brief at 5. However, APWU cannot deny that they are consistent with Commission precedent. APWU's witness provided no testimony regarding any business that is required to fulfill public services obligations similar to those of the Postal Service, or to price its products and services in a manner consistent with the pricing policies of the Postal Reorganization Act.

C. APWU Mischaracterizes The Postal Service's Additional-Ounce Costing Testimony.

At page 21 of its brief, APWU mischaracterizes the analysis underlying the Postal Service's proposal to establish a lower additional-ounce rate for workshare rate categories. APWU argues that the cost study underlying witness Robinson's rate design shows "a difference of 0.15 cents for the average piece." This assertion is not correct. The 0.15-cent difference is the difference between the cost of an additional ounce for single-piece and presort. In other words, it is derived from the costs per additional ounce, not from per-piece costs. This was clear from witness Robinson's

testimony (USPS-T-29 at 25) and in the response of witness Schenk (USPS-T-43) to Question 10 of Presiding Officer's Information Request No. 8. Tr. 14/5644.

APWU also argues that the proposed additional-ounce rate differential should not be recommended "absent a meaningful showing of a true cost difference." APWU Brief at 21. However, such information was provided by the Postal Service in response to VP/USPS-4, especially in Attachment A, which shows the additional-ounce costs for single-piece and presort broken down by cost pool for 2-3 ounce pieces, compared to 0-1 ounce pieces. See Tr. 10C/3697-99.¹² These data clearly show that costs for certain cost pools (OCR, manual letters, opening unit, platform, and pouching) are higher for single-piece additional ounces than for presort additional ounces.

Finally, APWU argues that the "difference of 0.15 cents is not meaningful." This argument is nothing more than a repetition of the assertion found in APWU witness Riley's testimony, Tr. 12/4862. Witness Riley performed no analysis or test to provide a foundation for his assertion. The Postal Service, however, did provide data showing that the individual additional-ounce costs for pieces over an ounce have low coefficients of variation for both single-piece and presort, which lends credibility to these cost estimates. See Tr. 11B/4435-4436. The cost data are "meaningful." The difference is "true."

¹² The copy of the designated response in the transcript does not contain Attachment A, which was filed with the response on November 27, 2001. The Postal Service assumes that the Attachment is considered incorporated by reference at this citation in the evidentiary record.

IV. The Commission Has Not Deprived APWU of Due Process.

In its Initial Brief, APWU argues that its due process rights have been compromised in this proceeding. (APWU Brief at 22-30). In this argument, APWU focuses almost exclusively on the Commission's treatment of the surrebuttal testimony filed on behalf of parties defending the settlement rates for First-Class Mail. APWU notes that it had proposed procedural measures that would provide due process from its perspective, but that "APWU's proposals concerning rebuttal testimony and surrebuttal were not adopted." APWU Brief at 23.

Originally, APWU proposed that it be given an opportunity for discovery and rebuttal regarding any testimony that the First-Class Mail interests might file challenging APWU's position on the relationship between the proposed discounts and avoided costs. APWU contended that such testimony would "normally have been presented in case-in-chief of intervenors."¹³ The Presiding Officer, however, rejected that view. In a relatively straightforward application of the Commission's rules and practice, he rightly concluded that, to the extent the intervenors would challenge APWU's testimony opposing settlement, their testimony "cannot be characterized fairly as the case-in-chief of any

¹³American Postal Workers Union, AFL-CIO Initial Reply to Motion of the United States Postal Service for the Establishment of a Procedural Mechanism and Schedule Governing Further Proceedings in Light of the Settlement and Suggestions for Procedural Mechanisms and Schedules, Docket No. R2001-1, at 4 (Jan. 24, 2002).

participant.”¹⁴ He established a schedule that provided neither for discovery against the intervenors nor “surrebuttal” testimony by APWU. Subsequently, in disposing of several APWU motions to strike the intervenors’ surrebuttal testimony, the Commission again rejected APWU’s contention that such testimony was beyond the bounds of proper surrebuttal. The Commission noted several instances in which APWU’s witness Riley, through his own statements, had created the foundation for the intervenors’ testimony.¹⁵

In its Initial Brief, APWU has not abandoned its argument that the intervenors’ testimonies, in effect, amounted to cases-in-chief, and that they should have been stricken. Initial Brief at 28-29. APWU makes no attempt, however, to refute the basis for the Commission’s order refusing to strike, namely, that APWU’s own witness presented testimony that the surrebuttal testimony directly addressed. Beyond that conclusion, APWU now appears to argue principally that it was deprived of due process, because it was not given enough time to understand, evaluate, and test the surrebuttal. APWU distills this argument as follows:

In light of the type of testimony that was filed by other intervenors in this case as “surrebuttal” testimony, the failure of the schedule and procedures to provide sufficient time and mechanisms for the APWU to respond has compromised the APWU’s due process rights in this case.

Initial Brief at 23.

¹⁴ Presiding Officer’s Ruling Establishing the Procedural Schedule for Consideration of the Proposed Stipulation and Agreement, POR No. R2001-1/43, Docket No. R2001-1, at 4 (Jan. 31, 2002).

¹⁵ Order Resolving Motions to Strike Surrebuttal Testimony, Order No. 1337, Docket No. R2001-1, at 2-5 (Feb. 27, 2002).

In this important respect, APWU's due process argument is entirely contingent. APWU has not demonstrated that the Commission misinterpreted or misapplied its rules and precedent in declining to schedule a surrebuttal stage for APWU. APWU has not effectively challenged the Commission's conclusion that witness Riley provided a substantive basis for the intervenors to file rebuttal. And, it has certainly not established that it has otherwise not been given an opportunity to challenge the primary focus of its opposition – the settlement.¹⁶ What APWU argues primarily is that, if the Commission were to rely on the testimony that it refused to strike, APWU would be prejudiced, because it was not given an adequate opportunity to understand it.

Even if the procedural deficiency APWU describes were correct, however, it would be wrong to conclude that any reliance on the intervenors' testimony would automatically deprive APWU of due process. Admittedly, intervenor

¹⁶ As we argued in the Postal Service's Initial Brief, the Commission has fully met its obligations to afford APWU a fair hearing. Postal Service Initial Brief at I-10-11. With regard to the issue of the appropriate level of cost avoidance – which the surrebuttal evidence principally addresses -- it can be argued that APWU failed effectively to raise a material factual issue that requires any further hearing. Witness Riley repeatedly testified that he, in effect, took the Postal Service's estimates of avoided costs as a given. Tr. 12/4864, 4903-05, 4915. Furthermore, he professed that his primary purpose was to "talk about policy, not differences in methodology." *Id.* at 4914; *see also Id.* at 4927 ("The purpose of my testimony is to testify about the policy of setting discounts at 80 to 100 percent...."). He characterized his analysis as not dependent on any particular level of cost avoidance. He stated: "My advice to the Commission is *whatever they determine to be the avoided costs*, to take 80 percent of that and use that to set the discounts...." *Id.* at 4907(emphasis added). To the extent that he raised questions about the accuracy of the Postal Service's cost avoidance estimates (see instances cited in Order No. 1337), his testimony was general and vague, and he did not support any alternative estimates of his own. In this regard, the Commission has concluded that the onus is on the opponent of a settlement to

witnesses have raised questions regarding the appropriateness of the methodologies employed by Postal Service's witness Miller to interpret the underlying data used in his analysis.¹⁷ Apparently responding to APWU witness Riley's assertion that witness Miller may have *overstated* workshare cost avoidance (Tr. 12/4849-50), their testimonies have suggested that the workshare cost avoidance estimates provided by Postal Service witness Miller (USPS-T-22) may actually be *understated*. To support this conclusion, they have advanced alternative analytic methodologies, and have asserted that applying them to the same fundamental input data would yield different estimates of the postal costs avoided.¹⁸

establish the need for a hearing. See PRC Op. MC84-2, at 9 and n. 9 (Dec. 21, 1984).

¹⁷The Postal Service does not support the conclusions drawn by the intervenors. Furthermore, as a practical matter and legally, all of the settlement parties are bound by the nonprecedential compromise, embodied in the Stipulation and Agreement, that the Postal Service's evidence constitutes substantial support for the settlement proposals. Stipulation and Agreement, ¶ II.3, at 3. If only because the intervenors' contentions conflict with that fundamental element of the settlement, the Commission would be justified in disregarding the alternative bases for support offered by the intervenors, and in relying exclusively on the Postal Service's case to support recommendation of the settlement.

¹⁸ As noted above, ABA&NAPM witness Clifton (ABA&NAPM-SRT-T-1; Tr. 13/5269 *et seq.*), Keyspan witness Bentley (NEED TO FINISH CITE) (KE-SRT-1; Tr. 13/5338 *et seq.*), and MMA witness Bentley (MMA-SRT-1; Tr. 13/5156 *et seq.*) offered a variety of methodologies to analyze First-Class Mail costs, in an effort to refute Mr. Riley's assertion that the Postal Service's estimates of workshare cost avoidance may be overstated. National Association of Presort Mailers witness Gillotte (NAPM-SRT-T-1; Tr. 13/5035-36) and Major Mailers Association witness Crider (MMA-SRT-2; Tr. 13/5101) both urged the Commission to expand the definition of worksharing cost avoidance to include consideration of workshare mailer participation on the Postal Service's Move Update program, and other factors.

In this regard, the intervenors advocate, in part, that the Commission could validate the settlement proposals independently, without relying explicitly on witness Miller's results, by applying methodologies approved in prior cases to the most recent input data presented by the Postal Service on the record of the current proceeding. This approach would be consistent with the Commission's approach in previous cases, where it has elected to rely on an established methodology, rather than on a proposed new methodology or its results.¹⁹ To the extent that the intervenors have advocated this approach, their testimonies would not necessarily conflict with the conclusion embodied in the settlement agreement that the record established by the Postal Service's evidence substantially supports the settlement proposals.

This option would presumably have been available to the Commission, whether or not intervenor witnesses had testified pointing in that direction. In fact, in this proceeding, the record basis for this type of approach can be found within the evidence generated during presentation of the Postal Service's case. See Tr. 7/1621-26; Tr. 10A/2862.

It is therefore at least premature and unfounded to conclude that the Commission has deprived APWU of due process by failing to give it an adequate chance to understand and challenge the surrebuttal testimony.²⁰ As the

¹⁹ For example, in Docket No. R2000-1, the Commission rejected a proposed new analysis of city carrier costs and returned to the PRC's established methodology. See PRC Op. R2000-1, Vol. 1, at 109-36.

²⁰ Due process "is not a technical conception with a fixed constant unrelated to time place and circumstances . . . [rather] . . . due process is flexible and calls for such procedural protections as the particular situation demands." Matthews v. Eldridge, 424 U.S. 319, 334 (1976) (citations and quotations omitted).

Commission has said many times before, it is competent to give such testimony the weight it deserves. Furthermore, the surrebuttal testimony could be relied upon partially to support settlement, without accepting the results of the analyses that APWU opposes. The Commission should therefore reject APWU's challenge to the settlement on due process grounds, and adopt the settlement agreement on the basis of the evidence and argument presented in the Postal Service's Initial Brief and above.

V. There Also Are Compelling Substantive Reasons for Not Basing Rates on the Alternative Surrebuttal Cost Analyses.

As explained above in Section IV, the Commission has decision options which, if carefully exercised, should serve to eliminate the possibility of APWU having any basis for reviving its due process concerns before the Governors of the United States Postal Service during the 39 C.F.R. § 9.2 comment period immediately following the Docket No. R2001-1 recommended decision. That notwithstanding, there also are a variety of substantive reasons why the Commission should not rely upon the alternative cost estimates of witnesses Bentley and Clifton as a basis for ratemaking in this proceeding.²¹

A. The Surrebuttal Bulk Workshare Cost Avoidance Analyses Are Inferior to Witness Miller's Testimony.

1. All of the conflicting estimates cannot be the most reliable.

At page 4 of their Brief, ABA&NAPM claim that an "accurate measure" of cost avoidance will support the settlement rates contained in the Stipulation and Agreement. The use of the term "accurate measure" would seem to imply a belief that one set of "accurate" worksharing related savings estimates exists. However, ABA&NAPM undermine their argument by pointing to four "accurate," yet distinct estimates in Table 1 on page 6 of their Brief. All that Table 6 makes clear is that different cost methodologies will result in different worksharing related savings estimates.

²¹ The Commission might deem it appropriate to acknowledge the intervenor surrebuttal cost avoidance estimates for the limited purpose of establishing that there was controversy surrounding Mr. Riley's assertion at Tr. 12/4849-50 that the Postal Service's cost avoidance estimates might be overstated.

2. Witness Miller's methodological changes are appropriate.

MMA claims that "the changes that Mr. Miller made in the Commission's accepted methods for measuring workshare cost savings make his resulting cost savings an inappropriate yardstick against which to judge the S&A discounts."

MMA Brief at 14-15. The methodology that is employed in a given cost study obviously can affect its results. However, Postal Service witness Miller (USPS-T-22) only made two changes to his Docket No. R2000-1 methodology. First, he accepted the Commission's Docket No. R2000-1 cost pool classifications, with the exception that he reclassifies the "1SUPPF1" and "1SUPPF4" cost pools²² as "non-worksharing related." USPS-T-22 at 9-10.

Second, witness Miller refined the Bulk Metered Mail (BMM) letters delivery unit cost proxy. In response to the availability of more refined data in this docket, he selected the Nonautomation Machinable Mixed AADC Presort letters delivery unit cost estimate as the proxy for BMM letters. USPS-T-22 at 20.²³

²² Which include tasks not directly affected by the presorting and/or prebarcoding of mail.

²³ In addition, both the ABA&NAPM and the MMA seem to take issue with the BMM letters benchmark and the Postal Service's approach to volume variability. The Postal Service addressed the benchmark issue in its Initial Brief at V-14. As for the issue of volume variability, all the Postal Service can do is wonder why parties to the Stipulation and Agreement would contest the non-binding use of the Postal Service's methodology in the current docket.

3. Task-based analysis is a cornerstone of accurate cost avoidance measurement.

Unlike the Postal Service, neither the ABA&NAPM nor the MMA have provided any logical, task-based rationale for supporting their positions concerning these areas of dispute. ABA&NAPM witness Clifton and MMA witness Bentley provided no logical, task-based reasons for including the "1SUPPF1" and "1SUPPF4" cost pools in the worksharing related savings estimates.²⁴ Neither intervenor surrebuttal witness offered a logical, task-based reason for rejecting the Nonautomation Machinable Mixed AADC Presort letters delivery unit cost estimate as the proxy for BMM letters. Neither witness provided a persuasive reason for rejection of Bulk Metered Mail (BMM) letters as the benchmark for the First-Class Mail presort letters rate categories.

Their approaches appear to be purely result-oriented. For example, when discussing the aforementioned pair of cost pools, MMA witness Bentley stated, "I do know that if the letters are work shared, the letter -- the cost in those cost pools are going to be lower than they are if they are metered." Tr. 13/ 5241. The specific value for these two cost pools is greater for BMM letters than it is for automation presort letters. Consequently, in his view, these cost pools must be worksharing related. Likewise, ABA&NAPM witness Clifton abandoned his Docket No. R2000-1 support for the Postal Service's approach to volume

²⁴ In fact, MMA witness Bentley demonstrated a complete lack of knowledge regarding the tasks represented by these cost pools when he confessed, "I don't know what that means myself." Tr. 13/5241.

variability in favor of the "Commission-approved" cost methodology in Docket No. R2001-1.²⁵ One cannot help but wonder whether it is because the Commission's approach now yields higher savings estimates.

4. Claims that the Commission has rejected witness Miller's methodology are exaggerated.

ABA&NAPM further assert on page 12 of their Brief that "Mr. Miller utilizes cost avoidance methodology which has been expressly rejected by the Commission in several cases, including the most recent general rate case, R2000-1." MMA makes a similar accusation on page 15 of its Brief, when it states that "a fundamental problem with Mr. Miller's approach is that the Commission rejected significant portions of his analysis." Neither claim is a fair representation of reality.

Contrary to the ABA&NAPM assertion, witness Miller has offered a refined cost methodology for First-Class Mail workshare letters in only one previous case, Docket No. R2000-1. In that docket, he classified cost pools as being "worksharing related," using a task-based rationale. Docket No. R2000-1, USPS-T-24. In that proceeding, the Commission ultimately accepted the concept that all cost pools are not necessarily affected by worksharing. In regard to the

²⁵ In fact, none of the savings estimates on the record, including those in Table 1 of the ABA&NAPM Brief, rely on the Docket No. R2000-1 "Commission-approved" methodology. In that docket, the Commission reduced the value of the "1CANCMMP" cost pool by two-thirds of its original value. In the current docket, no such adjustments were made. Using the Postal Service volume variability methodology, such an adjustment would have reduced the worksharing related savings estimates for each rate category by 0.445 cents ($2/3 * 0.668$ cents).

specific cost pool classifications, the Commission accepted some of witness Miller's cost pool reclassifications, while rejecting others. See PRC Op. R2000-1, at 241, 5088-91.

In the current case, the Postal Service accepted the Commission's Docket No. R2000-1 cost pool classifications, with the exception of the "1SUPPF1" and "1SUPPF4" cost pools. Without explanation, ABA&NAPM merely declares them "relevant to worksharing." ABA&NAPM Initial Brief at 6, n.4. To the contrary, see USPS-T-22 at 9-10. It was ABA&NAPM witness Clifton and MMA witness Bentley who failed to offer any substantive rebuttal to witness Miller's testimony on this point.

In the current docket, the only other refinement witness Miller made to his Docket No. R2000-1 cost methodology concerned the adoption of Nonautomation Mixed AADC Presort letters as the delivery unit cost proxy for Bulk Metered Mail letters.²⁶ Because this refinement had not been presented to or evaluated by the Commission in earlier proceedings, there is no basis for the claims that the Commission "rejected" it in the past. Both ABA&NAPM witness Clifton and MMA witness Bentley failed to provide any persuasive reason why the Commission should ignore the opportunity to make a methodological change based upon the current availability of refined data.

Contrary to the assertions of witnesses Clifton and Bentley, it is possible

²⁶ For a summary of the Postal Service's explanation of the validity of using the Nonautomation Machinable Mixed AADC Presort letters delivery unit cost proxy, see the record evidence cited in the Postal Service Initial Brief at V-16-17.

that the Postal Service's First-Class Mail workshare savings estimates measured in this docket could be somewhat overstated, given that the BMM letters mail processing unit cost estimate represents the costs for all metered letters.

Metered letters are not exclusively machinable (Tr. 14/5535), are often entered in packages bundles (USPS-T-22 at 20), and can contain handwritten addresses.

See Tr. 14/5595. All three characteristics would result in higher mail processing costs, when compared to the "cleaner" BMM subset. In addition, several cost pools that have been classified as "worksharing related fixed" cost pools likely represent at least some tasks that would be required to process metered letters, but not BMM letters. Tr. 14/5527-31. It is interesting to note that 30-40 percent of the worksharing related savings estimates are based on the difference between the benchmark and rate category "worksharing related fixed" cost pools alone. The tasks represented by these cost pools are not included in the cost models. See Tr. 14/5531,5533.

Finally, ABA&NAPM also attempt to use the CRA "full cost difference" that exists between First-Class Mail single-piece letters and First-Class Mail presort letters as support for the claim that "cost avoidance is increasing." ABA&NAPM Brief at 15. The Commission has previously stated its view that full cost difference methodologies result in cost differentials that are "overinclusive." PRC Op. MC95-1 at IV-99, ¶4220. The cost differentials referenced by the ABA&NAPM include costs well beyond the avoided mail processing and delivery unit cost estimates that the Commission has historically relied upon as a basis for establishing First-Class Mail workshare letters discounts.

B. The Postal Service Analysis of QBRM Cost Avoidance Is Superior to the KeySpan Analysis.

1. The return to the Docket No. R97-1 methodology was justified.

On page 3 of their Brief, KeySpan *et al.* argue that Postal Service witness Miller testified that "the derived QBRM cost savings had plummeted from 3.4 cents in Docket No. R2000-1 to just 0.85 cents in this case." To the contrary, witness Miller testified that the Postal Service's Docket No. R2000-1 QBRM cost study was flawed. USPS-T-22 at 26. His review of the Postal Service's Docket No. R2000-1 costing approach led him to conclude that a more limited analysis, similar to the analysis he conducted in Docket No. R97-1, was more appropriate.

Furthermore, witness Miller explained that it also was proper to evaluate the impact that improved Multi Line Optical Character Reader Input Sub System/ Remote Computer Read (MLOCR-ISS/RCR) finalization rates have had on the worksharing related savings estimates over time. USPS-T-22 at 27. The MLOCR-ISS/RCR finalization rate forecast in the Docket No. R2001-1 test year (82.77 percent) yielded a savings estimate of 1.647 cents. USPS-T-22 at 26-27.

Such a result is in line with improvements in letter and card processing, such as the increased Remote Computer Read (RCR) finalization rate. See Tr. 14/5481-5485.

KeySpan witness Bentley, however, preferred a state of denial to a state of improved cost estimation. He dismissed witness Miller's revised methodology as "outdated." Tr. 13/5344. Witness Bentley provided no rationale to refute

witness Miller's explanation of why a more limited analysis was more appropriate. Instead, despite warnings by witness Miller regarding limitations inherent in using cost models for purposes for which they were not suited (Tr. 14/5463, 5567-68), Mr. Bentley attempted to invalidate Mr. Miller's cost models by making erroneous assumptions regarding mail migrating from one category to another, without considering that -- had such a migration actually occurred -- the cost model input data also would have changed. Tr.13/5348. Furthermore, witness Bentley made an invalid comparison to the costs for other First-Class categories, which are calculated using cost methodologies that differ from that used in the QBRM cost study. Tr. 13/5350,5355.

The rationale for using a more limited analysis, such as that presented by witness Miller (USPS-T-22), is quite simple. A utility that provides QBRM mail pieces to its customers for the purposes of remittance payment can be used as an example. Such an extremely high volume remittance recipient would likely have its mail isolated on the automation outgoing primary operation, the first operation in which it is processed after being forwarded from cancellation operations. Were these mail pieces to migrate to a handwritten reply mail piece, the volume would stay the same. As witness Miller indicated, "volume dictates mail flow." Tr. 14/5470. Consequently, the handwritten reply mail pieces would likely be isolated in the outgoing Output Sub System (OSS) operation where a barcode is applied to that mail piece based on the Remote Bar Coding System (RBCS) result. Again, this would be the first operation in which these mail pieces would be processed (excluding the RCR and Remote Encoding Center, if

required), after being forwarded from cancellation operations. See Tr. 14/5467-72. This makes clear that a more limited analysis, such as that presented by witness Miller (USPS-T-22), is appropriate, because the only task differences that would exist between the benchmark handwritten piece and the QBRM piece concern the additional tasks required to apply a barcode to the former.

2. Witness Bentley's method relied almost exclusively on CRA adjustment factors.

Witness Bentley's worksharing related savings estimate was almost completely dependent on the CRA adjustment factors he used in his analysis. The model cost difference he measured between a handwritten reply mail piece and a QBRM mail piece was a mere 0.30 cents. Consequently, 4.73 cents of his 5.03-cent worksharing related savings estimate (94 percent) is caused by CRA adjustment factors alone.²⁷

In contrast, witness Miller's calculations were more reasonable. Despite the fact that his analysis was much more limited than that of witness Bentley, Mr. Miller calculated a larger model cost difference of 1.092 cents. Consequently, 0.555 cents of his 1.647-cent worksharing related savings estimate (34 percent) is caused by CRA adjustment factors alone. USPS LR-J-60 at 10.

Witness Miller applied the Bulk Metered Mail (BMM) letters CRA adjustment factor to both the handwritten reply mail piece and QBRM mail piece model cost estimates, before he calculated the worksharing related savings estimate. He explained that he used this CRA adjustment factor, because both mail categories

²⁷ Tr. 13/5347.

are also subsets of the First-Class Mail single-piece rate category, as is BMM letters. Tr. 14/5443. In fact, this CRA adjustment factor is likely high, because the BMM letters cost model is being reconciled to a CRA mail processing unit cost estimate that represents all metered letters. See USPS-T-22 at 20. Unlike BMM letters, metered letters are not necessarily machinable (Tr. 14/5535), are often entered in packages ("bundles") (USPS-T-22 at 20), and can contain handwritten addresses. Tr. 14/5595. The soundness of witness Miller's approach is self-evident, given that QBRM mail pieces and automation presort mail pieces have distinct characteristics. Tr. 14/5444.

Despite these explanations, witness Bentley applied the BMM letters CRA adjustment factor to the handwritten reply mail piece model cost estimate, while applying the First-Class Mail automation presort letters CRA adjustment factor to the QBRM mail piece model cost estimate. Tr. 13/5347. Consequently, the CRA adjustment factors witness Bentley used are responsible for 94 percent of his worksharing related savings estimate, as described above. An analysis that measures a cost avoidance in which 94 percent of the savings is based on adjustment factors alone should not be relied upon by the Commission.

VI CONCLUSION.

For the reasons stated above, the rates for postal services, fees for special services, and the modifications of the domestic mail classification schedule contained in the Stipulation and Agreement are supported by the evidentiary record and are in accord with the applicable provisions of the Postal Reorganization Act.

WHEREFORE, the Postal Service requests that the Postal Rate Commission recommend under 39 U.S.C. § 3624(d) the rates and fees and changes in the domestic mail classification schedule contained in the Stipulation and Agreement.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

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